

***United States Court of Appeals
for the Second Circuit***



**BRIEF FOR
APPELLEE**

76-6055

To be argued by

R. MARSHALL WITTEN

**United States Court of Appeals
FOR THE SECOND CIRCUIT**

Docket No. 76-6055

FRANCESCO GALESI,

Plaintiff-Appellee,

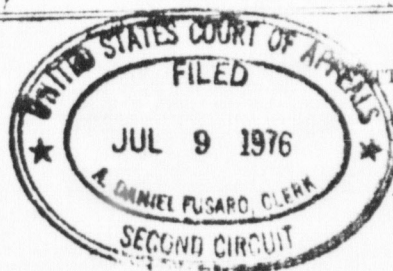
v.

UNITED STATES OF AMERICA,
INTERNAL REVENUE SERVICE,

Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE
DISTRICT OF VERMONT

**BRIEF FOR THE APPELLEE
FRANCESCO GALESI**



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BRIEF FOR THE APPELLEE
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Statement of the Issue

Whether a Vermont foreclosure action is a "judicial proceeding" within the meaning of 26 USC 7425(a)?

Statement of the Case

I. Prior Proceeding.

On February 27, 1975, in accordance with prescribed Vermont procedure, Francesco Galesi commenced a civil action for declaratory judgment in Bennington Superior Court to quiet title to lands owned by him in Manchester, Vermont (The Equinox property). Pursuant to 28 USC

1444 the United States of America removed the case to the United States District Court for the District of Vermont. The parties stipulated below that the facts giving rise to their competing claims were in all material respects undisputed and agreed that summary judgment was the appropriate disposition by the District Court.

The District Court granted Plaintiff's motion for summary judgment and denied Defendant's motion for summary judgment. Defendant has appealed to this Court.

II. Facts.

The Chemical Bank held two mortgages on the Equinox property and on September 10, 1973 it commenced suit (*Chemical Bank v. The Equinox House, Inc., et al.*, Benn. Super. Ct., Civil No. C94-73 Be, Feb. 11, 1974) and filed a copy of the foreclosure complaint in the Manchester Town Clerk's Office as required by 12 VSA 4523 which provides in part as follows:

(b) The Plaintiff shall file a copy of the complaint in the town clerk's office in each town where the mortgaged property is located. The clerk of the town shall minute on the margin of the record of the mortgage that a copy of foreclosure proceedings on the mortgage is filed. The filing shall be sufficient notice of the pendency of the action to all persons who acquire any interest or lien on the mortgaged premises between the dates of filing the copy of foreclosure and the recording of the final judgment in the proceedings. Without further notice or service, those persons shall be bound by the judgment entered in the cause and be foreclosed from all rights or equity in the premises as completely as though they had been parties in the original action.

Chemical Bank joined as defendants in the foreclosure proceeding all junior mortgagees and other lien holders of record on the date of filing suit.

Eight days later, on September 18, 1973, the Internal Revenue Service filed a Notice of Tax Lien against The Equinox House, Inc. in the Manchester Town Clerk's Office. The United States did not avail itself of its right to intervene in the pending Chemical Bank foreclosure proceedings in Bennington Superior Court under 26 USC 7424:

If the United States is not a party to a civil action or suit, the United States may intervene in such action or suit to assert any lien arising under this title on the property which is the subject of such action or suit. The provisions of section 2410 of title 28 of the United States Code (except subsection (b)) and of section 1444 of title 28 of the United States Code shall apply in any case in which the United States intervenes as if the United States had originally been named a defendant in such action or suit. In any case in which the application of the United States to intervene is denied, the adjudication in such civil action or suit shall have no effect upon such lien.

On February 11, 1974, the Bennington Superior Court entered its Judgment Order of Foreclosure and assigned specific redemption dates for the other mortgagees and lienors. On June 12, 1974, Plaintiff, as assignee of a junior mortgagee, timely redeemed the property by paying the sum of \$1,281,045.54 to the Deputy Clerk of the Superior Court for the benefit of the Chemical Bank. The foreclosure proceedings complied with the local law in all respects.

Thereafter, the Internal Revenue Service posted a notice of public sale of the Equinox property to satisfy its tax lien, claiming it had not been discharged in the state court proceeding. The sale was postponed at the Plaintiff's request to allow the parties to discuss their respective

rights in the property. Plaintiff found the discussions unsatisfactory, and, as a result, brought this action for declaratory judgment in the state court.

ARGUMENT

A Vermont real estate foreclosure action is a civil action or suit in a state court having jurisdiction to foreclose a mortgage upon real property on which the United States has or claims a lien as described in 28 USC 2410(a) and required by 26 USC 7425(a).

In Vermont there is only one form of action—a “civil action”. V.R. Civ. P. 2. Foreclosure is a civil action. A Vermont real estate foreclosure is a plenary judicial proceeding involving all the procedural safeguards available in every Vermont civil action.*

Vermont requires notice, specific pleadings, an opportunity for the defendant to be heard on the merits (including the right to cross-examine witnesses under oath) and judgment as essential elements of a civil action—elements that are the essence of a judicial proceeding. To focus on the fact that the foreclosure action in this case may be characterized as a “strict foreclosure” proceeding is to miss the point of the intended reforms in the Federal Tax Lien Act of 1966. The critical distinction is not between “strict foreclosure” and other types of foreclosure proceedings,

* In Vermont 12 VSA, Chapter 163, subchapter 6 and V.R. Civ. P. 80.1 govern real estate foreclosures. The plaintiff serves a summons and complaint upon all those holding or claiming an interest of record in the property. If the Plaintiff so elects he may move for summary judgment under V.R. Civ. P. 56, thereby requiring a defendant not only to appear and answer but also to interpose an affidavit of defense. The parties are entitled to a full trial on the merits, with findings of fact, a judgment order, redemption dates and a writ of possession. In short, a Vermont foreclosure proceeding invokes the full panoply of protections afforded in all civil actions. V.R. Civ. P. 13(a) (compulsory counterclaims) governs defendant's responsive pleadings.

including judicial sales; rather it turns on whether the strict foreclosure action, or the sale, as the case might be, emanates from a judicial proceeding or results from purely private action. In some jurisdictions a mortgagee by purely private action without resort to the courts may foreclose all junior interests. Powell, *Real Property*, ¶ 468-70. The opportunity to abuse the system outside the protection of judicial proceedings is obvious, laying the groundwork for a valid legislative distinction between judicial versus non-judicial foreclosure of mortgages. Hence Congress drew a sharp distinction in 26 USC 7425(a) and 7425(b).

Congress did not design the Tax Lien Act of 1966 to give the United States relief under the instant facts. 26 USC 7425(a) clearly provides that a *judgment* in any civil action or suit described in 28 USC 2410(a) or a judicial sale pursuant to such judgment with respect to property on which the United States has or claims a lien shall discharge such lien as provided by the law of the place where such property is situated "if no notice of such lien has been filed in the place provided by law for such filing at the time such action or suit is commenced".

Though the statute clearly says a "judgment . . . or a judicial sale pursuant to such judgment . . ." the government chooses to ignore the applicable first portion of the statute and relies instead on the inapposite portion which, in turn, triggers a line of argument and examination of cases not on point.

The civil action or suit described in 28 USC 2410(a) is "any civil action or suit . . . in any state court having jurisdiction . . . to foreclose a mortgage or other lien upon . . . real . . . property on which the United States has or claims a . . . lien."

The legislative history of section 7425(a) supports this interpretation. Indeed, on February 12, 1976 the Commissioner of Internal Revenue himself, in a communication to the House Committee on Ways and Means, stated that:

... the bill adds a new section 7425 to the Internal Revenue Code. Subsection (a) of that section provides that the lien of the United States may not be extinguished by a judicial foreclosure unless the United States is joined, if notice of the lien of the United States is on file on the date the foreclosure action is commenced. *Thus, a litigant need only check the record for federal tax liens on the date of commencement of the action.* [emphasis added.] Hearings, House Committee on Ways and Means, 89th Cong., 2nd Sess., p. 57.

The Temporary Treasury Regulations 400.4-1(a) also recognize the distinction:

Section 7425(a) contains provisions relating to the discharge of a lien in the judicial proceedings described in Subsection (a) of Section 2410 of Title 28 . . . These judicial proceedings are plenary in nature and proceed on formal pleadings.

The four examples cited in Temporary Treasury Regulations 400.4-1(b)(2) clearly relate to the 7425(b) situations where there is a nonjudicial enforcement of rights based upon either "an instrument creating a lien on the property sold" or "a statutory lien on the property sold". None of the examples approximate a Vermont civil action to foreclose a mortgage on real property.

The government places great reliance on Example (3) which alone has the "strict foreclosure" feature in common with Vermont. In Example (3), however, the mortgagee's entry on the property is without benefit of judicial writ or process. The mortgagee's attorney files a certificate of entry in the registrar's office, and his action divests the interests of the mortgagor and junior lienors automatically one year after such filing. None of the plenary elements of a

Vermont judicial proceeding—formal pleadings, opportunity to examine witnesses under oath, and the independent judgment of the court based on the evidence—are found in Example (3). The Vermont procedure (12 VSA 4523) affords at the very least constructive notice, with the opportunity for actual notice, to all the world not actually filed the date the suit is commenced; 26 USC 7424 and 12 VSA 4524* allow the United States to intervene as a matter of right at any time, even after judgment. The local Internal Revenue Service Office did not do its homework. The government did not check the land records and utilize the powers of intervention that Congress and the Vermont Legislature provided.

Conclusion

The government is therefore bound by the unambiguous language of 7425(a). Under our facts a "litigant need only check the record for federal tax liens on the date of commencement of the action." Hearings, House Committee on Ways and Means, 89th Cong., 2nd Sess., p. 57. The judgment of the District Court should be affirmed.

Respectfully submitted,

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* § 4524. Supplemental judgment joining parties; recording

At any time, without further notice or service on the purchaser, mortgage or lien holder, upon filing certified copies of the deed, mortgage or attachment with the clerk of the court, any superior judge may sign a supplemental judgment specifically naming that party. Reference to the deed, mortgage or lien and the supplemental judgment may be filed in the town clerk's office for record, and it shall have the same force and effect as though that person had been made a party defendant in the original action.

UNITED STATES COURT OF APPEALS
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Docket No. 76-6055

Francesco Galesi,
Plaintiff Appellee.

V.

United States of America, Internal
Revenue Service,
Defendants Appellants

Affidavit
of
Service by Mail

STATE OF NEW YORK }
COUNTY OF New York } ss.:

Robert McElroy , being duly sworn,
deposes and says:

I am over the age of twenty-one years and reside at
277 Avenue C , in the
Borough of Manhattan , City of New York. On the
9th day of July , 1976 , at o'clock ,

I served 3 copies of the Brief for the Appellee Francesco Galesi

in the above-entitled action on:

Scott P. Crampton, Esq.
Assistant Attorney General-Tax Division
United States Department of Justice
Washington, D.C. 20530

Hon. George W.F. Cook
United States Attorney
Federal Building
Rutland, Vermont 05701

the attorneys for the Defendants Appellants

in the said action, by depositing said copies, securely wrapped properly addressed, and postage fully prepaid, in a post office box regularly maintained by the U. S. Government in the post office at 90 Church Street, in the Borough of Manhattan, City of New York.

Robert Paul Elroy

Sworn to before me this ^{9th}
day of *July*, 19*76* }

Greg Weiss

JERRY M. WEISS
Notary Public, State of New York
No. 407335
Commission Expires March 30, 1979